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Proposed Counsel for Debtor

UNITED STATES BANKRUPTCY COURT
DISTRICT OF ARIZONA

In re:

ARCTIC CATERING, INC.

Debtors.

Chapter 11 Proceeding

Case No. 2:18-bk-13118-EPB

**EMERGENCY MOTION FOR
ORDER AUTHORIZING PAYMENT
OF PRE-PETITION WAGES,
SALARIES, EMPLOYEE BENEFITS,
AND RELATED ITEMS**

Hearing Date: October 29, 2018

Hearing Time: 2:30 p.m.

Courtroom: 601

**Location: 230 N 1st Ave, Phoenix, AZ
85003**

Arctic Catering, Inc., debtor and debtor-in-possession (the “**Debtor**”) in the above-referenced chapter 11 case (the “**Bankruptcy Case**”) respectfully submits this motion (the “**Wages Motion**”), under Sections¹ 105(a), 363, 507(a)(4), 541(b)(7), and 541(d) of the Bankruptcy Code, Bankruptcy Rules² 6003 and 6004, and Local Rule³ 4001-4(b), and requests this Court enter an order authorizing payment (i) of pre-petition wages, salaries, overtime pay (the “**Wages**”), as well as payments deducted from Employees’ paychecks

¹ As used herein, “**Section**” refers to a section of title 11 of chapter 11 of the United States Code, 11 U.S.C. §§ 101 *et seq.* (the “**Bankruptcy Code**”).

² As used herein, “**Bankruptcy Rule**” refers to a rule of the Federal Rules of Bankruptcy Procedure, Bankruptcy Rules 1001-9037.

³ As used herein, “**Local Rule**” refers to a rule of the Local Rules of Bankruptcy Procedure for the District of Arizona.

1 (the “**Deductions**”) on account of Employees’ benefit programs, and withholdings from
2 the Employees’ paychecks on account of various federal, state or local income, FICA,
3 Medicare, state disability, worker’s compensation and other taxes for remittance to the
4 appropriate federal, state or local taxing authority (collectively the “**Withholdings**,” and
5 together with the Wages, and Deductions, the “**Prepetition Compensation**”); (ii)
6 prepetition contributions to, and benefits under, employee benefit plans (collectively, the
7 “**Prepetition Benefits**”); and (iii) granting other related relief.

8 **Pursuant to Local Rule 4001-4(b)(7), the Debtor requests payment of Wages**
9 **for its President and Chief Executive Officer in the amount of \$8,571.43.**

10 The Debtor requests emergency approval of this Motion because the Debtor’s
11 reorganization efforts risk serious disruption without sustaining the work efforts of the
12 Debtor’s Employees. Put simply, the Debtor wants to make sure its Employees are
13 working hard and are able to concentrate on the job at hand rather than worrying about
14 getting paid during this chapter 11 case.

15 The Wages Motion is further supported by the (1) *Declaration of David Gonzales*
16 *in Support of First-Day Pleadings* (the “**Gonzales Declaration**”) filed contemporaneously
17 herewith; (2) the following Memorandum of Points and Authorities; (3) the documents
18 referenced herein; and (4) the entire record before the Court in this case. In support
19 hereof, the Debtor respectfully states as follows:

20 **MEMORANDUM OF POINTS AND AUTHORITIES**

21 **I. JURISDICTION AND VENUE**

22 1. This Court has subject matter jurisdiction over this Motion under 28 U.S.C.
23 §§ 157 and 1334, and the standing order of reference signed by Chief Judge Stephen M.
24 McNamee dated June 29, 2001, which order, among other things, refers bankruptcy cases
25 to the bankruptcy judges for the District of Arizona.

26 2. This matter constitutes a core proceeding within the meaning of 28 U.S.C. §
27 157(b)(2).

28 3. Venue is proper under 28 U.S.C. §§ 1408 and 1409.

1 **II. FACTUAL BACKGROUND**

2 **A. The Debtor's Business and the Chapter 11 Filing**

3 4. The Debtor, an Alaska corporation, was founded in 1973.

4 5. The Debtor is headquartered at 7373 E Doubletree Road, Suite 135,
5 Scottsdale 85258.

6 6. The President and Chief Executive Officer is David Gonzales.

7 7. The Debtor is a catering and support services company. Its main lines of
8 business are logistics support, food services, and facility management for employees at
9 remote camp and lodging centers of oil and gas companies around the country, with a
10 primary focus on the Northwest Alaskan frontier. The Debtor also designs remote camps
11 and related operations from the ground up.

12 8. In 2018, the Debtor has generated approximately \$16,679,234 in revenue to
13 date.

14 9. Since the commencement of the Bankruptcy Case, the Debtor has continued
15 in possession of its property and is operating and managing its business as debtor-in-
16 possession pursuant to Sections 1107(a) and 1108.

17 10. Additional information regarding the circumstances leading to the
18 commencement of this case and information relating to the Debtor's business is set forth in
19 detail in the Gonzales Declaration filed contemporaneously herewith.

20 **B. The Prepetition Compensation and Prepetition Benefits Owed to**
21 **Employees**

22 11. As of the Petition Date, the Debtor has 187 employees (the "**Employees**"). A
23 list of the Employees is attached as **Exhibit A**.

24 12. The Debtor's payroll is approximately \$220,000 per week. The Debtor pays
25 payroll on Wednesday each week for the previous week.

26 13. All of the Employees are owed or have accrued various sums of Prepetition
27 Compensation. The Prepetition Compensation remains unpaid on the Petition Date
28 because, among other things, (1) the Debtor commenced its Bankruptcy Case in the midst

1 of its customary payroll period, and (2) checks previously issued on account of Prepetition
2 Benefits obligations may not have been presented for payment, or may not have cleared
3 the banking system. Regarding the former, Wages for the period of 10/21/18 – 10/25/18
4 constitute Prepetition Compensation scheduled to be paid on 10/31/18.

5 14. The Debtor estimates that the total amount of unpaid Prepetition
6 Compensation for Employees was no more than \$139,139.57⁴, comprised of \$125,714.29
7 in pre-petition wages for 10/21/18 – 10/25/18, \$6,235.91 in manual payroll checks yet to
8 be cashed, \$6,452.05 in manual 401k funding, and \$767.32 in HSA funding.

9 15. The Debtor also owes certain of its Employees reimbursable expenses in the
10 amount of \$6,917.14 (the “**Expenses**”), as set forth in detail in **Exhibit B**.

11 **C. Prepetition Benefits**

12 16. The Prepetition Benefits relate to the Debtor’s employee benefit programs,
13 including: (i) plans maintained by the Debtor that provide medical, dental, vision,
14 prescription drug, life, accident and disability insurance; and (ii) a 401(k) retirement plan
15 for its Employees (collectively, the “**Benefit Programs**”).

16 17. Certain Prepetition Benefits were owed but remained unpaid as of the
17 Petition Date because various obligations under the Benefit Programs accrued either in
18 whole or in part prior to the Petition Date. The total amount for unpaid Prepetition
19 Benefits is less than \$5,000.00. The Debtor seeks authorization to pay all Prepetition
20 Benefits that, as of the Petition Date, had accrued but remained unpaid.

21 **III. LEGAL GROUNDS FOR RELIEF REQUESTED**

22 The payment of the Prepetition Compensation, Prepetition Benefits is warranted
23 under Sections 105(a), 363, 507(a)(4), 507(a)(5), 541(b)(7) and 541(d), and by decisions
24 from courts around the country.

25 **A. Employee Wages and Benefits Enjoy Priority Status under the**
26 **Bankruptcy Code**

27
28 ⁴ This amount includes the prepetition Wages sought for the Debtor’s President and Chief
Executive Officer.

1 Under Section 507(a)(4), employees receive a priority claim for:

2
3 allowed unsecured claims, but only to the extent of \$12,850 for
4 each individual or corporation, as the case may be, earned within
5 180 days before the date of the filing of the petition or the date
6 of the cessation of the debtor's business, whichever occurs first,
7 for —

8 (A) wages, salaries, or commissions, including vacation,
9 severance, and sick leave pay earned by an individual; or

10 (B) sales commissions earned by an individual or by a
11 corporation with only 1 employee, acting as an independent
12 contractor in the sale of goods or services for the debtor in the
13 ordinary course of the debtor's business if, and only if, during
14 the 12 months preceding that date, at least 75 percent of the
15 amount that the individual or corporation earned by acting as
16 an independent contractor in the sale of goods or services was
17 earned from the debtor

18 11 U.S.C. § 507(a)(4). In addition, under Section 507(a)(5), employees are granted a
19 priority claim for:

20 allowed unsecured claims for contributions to an employee
21 benefit plan —

22 (A) arising from services rendered within 180
23 days before the date of the filing of the petition or the
24 date of the
25 cessation of the debtor's business, whichever occurs first; but only

26 (B) for each such plan, to the extent of —

27 (i) the number of employees covered by
28 each such plan multiplied by \$12,850; less

(ii) the aggregate amount paid to such
employees under paragraph (4) of this subsection,
plus the aggregate amount paid by the estate on
behalf of such employees to any other employee
benefit plan.

11 U.S.C. § 507(a)(5).

Here, the Debtor the net amount of Prepetition Compensation, Expenses, and
Prepetition Benefits owing to or on account of its employees does not exceed the sum of
\$12,850 per employee, allowable as a priority claim under Sections 507(a)(4) and
507(a)(5). Therefore, authorizing the Debtor to pay these amounts would not deplete

1 funds that would otherwise be available to other unsecured creditors under a chapter 11
2 plan.

3 **B. Funds Held in Trust Are Not Available for General Distribution to**
4 **Creditors**

5 Section 541(d) of the Bankruptcy Code provides that “property in which the debtor
6 holds, as of the commencement of the case, only legal title and not an equitable interest”
7 becomes property of a debtor’s estate only to the extent of the debtor’s legal title therein.
8 11 U.S.C. § 541(d). It is well established that property a debtor holds in trust for another is
9 not property of the estate within the meaning of Section 541. *See Advent Mgmt. Corp. v.*
10 *Taylor Assocs. (In re Advent Mngmt. Corp.)*, 104 F.3d 293, 295 (9th Cir. 1997); *see also*
11 *Mitsui Mfrs. Bank v. Unicom Computer Corp. (In re Unicom Computer Corp.)*, 13 F.3d
12 321, 324 (9th Cir. 1994) (finding that funds that would be subject to a constructive trust
13 are not property of the estate under section 541(d)).

14 More specifically, it is well established under Section 541(d) that taxes collected on
15 behalf of taxing authorities are not property of the estate. *See Begier v. IRS*, 496 U.S. 53,
16 59 (1990) (holding that taxes such as excise taxes, FICA taxes and withholding taxes are
17 property held by the debtor in trust for another and, as such, do not constitute property of
18 the estate); *see also Texas Comptroller of Pub. Accounts v. Megafoods Stores, Inc. (In re*
19 *Megafoods Stores, Inc.)*, 163 F.3d 1063 (9th Cir. 1998) (finding that a debtor holds only
20 legal title in certain sales tax, and not an equitable interest, thus not property of
21 bankruptcy estate); *City of Farrell v. Sharon Steel Corp. (In re Sharon Steel Corp.)*, 41
22 F.3d 92, 98-103 (3d Cir. 1994) (finding that funds withheld from employees’ paychecks
23 may be subject to a trust, and thus are not property of a debtor’s estate, even where such
24 funds were commingled with the debtor’s other property). Accordingly, such funds are
25 not available for general distribution to a debtor’s creditors.

26 The Withholdings are held in trust for the benefit of the appropriate federal, state
27 or local taxing authorities. Likewise, certain of the Deductions also are held in trust for,
28 among others, the Debtor’s employees themselves. Thus, the Withholdings and

1 Deductions likely are not property of the Debtor's estate within the meaning of Section
2 541. As a result, the remittance of the Withholdings and Deductions is warranted because
3 it will not adversely affect the Debtor's estate or its creditors.

4 Further, many federal, state and local taxing authorities impose personal liability
5 on the officers and directors of entities responsible for collecting taxes from employees to
6 the extent any such taxes are collected but not remitted. Accordingly, if these amounts
7 remain unpaid, there is a risk that the Debtor's officers and directors may be subject to
8 lawsuits on account of any such nonpayment during the pendency of this Bankruptcy
9 Case. Such lawsuits obviously would constitute a significant distraction for officers and
10 directors at a time when they should be focused on the Debtor's efforts to (i) stabilize
11 their post-petition business operations and (ii) develop and implement a successful
12 bankruptcy strategy. To avoid the serious disruption of the Debtor's bankruptcy-related
13 efforts that could result from the nonpayment of any withholding taxes, the Debtor seeks
14 authority to remit all Withholdings collected on behalf of the employees, including
15 prepetition Withholdings, to the applicable taxing authorities to the extent that that they
16 have not already been remitted.

17 **C. The Doctrine of Necessity Provides a Further Basis for Granting the**
18 **Requested Relief**

19 Section 363(b)(1) provides that "[t]he trustee, after notice and a hearing, may use,
20 sell or lease, other than in the ordinary course of business, property of the estate." 11
21 U.S.C. § 363(b)(1). Section 105(a) provides:

22 The court may issue any order, process, or judgment that is
23 necessary or appropriate to carry out the provisions of this
24 title. No provision of this title providing for the raising of an
25 issue by a party in interest shall be construed to preclude the
26 court from, sua sponte, taking any action or making any
27 determination necessary or appropriate to enforce or
28 implement court orders or rules, or to prevent the abuse of
process.

1 11 U.S.C. § 105(a). Section 105(a) grants bankruptcy courts broad authority and
2 discretion to enforce the provisions of the Bankruptcy Code under equitable common law
3 principles.

4 Courts have long recognized the existence of the judicial power to authorize a
5 debtor to pay prepetition claims where such payment is essential to the continued
6 operations of the debtor. *In re Ionosphere Clubs, Inc.*, 98 B.R. 174, 176 (Bankr. S.D.
7 N.Y. 1989); *see also In re Columbia Gas Sys., Inc.*, 171 B.R. 189, 191-92 (Bankr. D. Del.
8 1994) (finding that a debtor is entitled to pay certain prepetition creditors upon a showing
9 that the payment is “essential to the continued operation of the business”) (citations
10 omitted. The United States Supreme Court first articulated the equitable common law
11 principle commonly referred to as the “doctrine of necessity” over 125 years ago in
12 *Miltenberger v. Logansport, C. & S.W.R. Co.*, 106 U.S. 286, 1 S. Ct. 140, 27 L. Ed. 117
13 (1882).

14 The bankruptcy court’s exercise of its authority under the “doctrine of necessity” is
15 appropriate to carry out specific statutory provisions of chapter 11, specifically Sections
16 1107(a), 1108 and 363(b)(1), which collectively authorize a debtor in possession to
17 maintain and operate the debtor’s business and use estate property outside of the ordinary
18 course of business. Indeed, a debtor in possession operating a business under Section
19 1108 of has a duty to protect and preserve the value of its business, and prepetition claims
20 may be paid if necessary to perform the debtor’s duty. *In re CoServ, L.L.C.*, 273 B.R.
21 487, 497 (Bankr. N.D. Tex. 2002) (“There are occasions when this duty can only be
22 fulfilled by the preplan satisfaction of a prepetition claim.”).

23 The Wages Motion satisfies the foregoing criteria, as the relief sought herein
24 plainly is essential to the continued operation of the Debtor. The immediate impairment
25 of the Debtor’s relationships with their employees and the irreparable harm to workforce
26 morale sure to attend any delay or disruption in the payments and benefits provided to
27 employees — at the very time when the dedication, confidence and cooperation of those
28

1 employees is most critical — will have an immediate harmful impact on the Debtor's
2 operations and the going concern value of the estates.

3 Maintaining the goodwill of the Debtor's employees and ensuring the availability
4 throughout the duration of this Bankruptcy Case will (i) assist the Debtor in maintaining
5 the necessary work atmosphere that the employees were used to pre-petition, and, in turn,
6 protect the going concern value of the estate and maximize the value ultimately available
7 to creditors and (ii) preserve the Debtor's relationships with customers and vendors that
8 will continue to provide value in connection with any going concern sale of the Debtor's
9 assets.

10 Furthermore, any harm resulting from the Debtor's failure to obtain the relief
11 requested herein would not be limited to the Debtor's estates. Because the amounts
12 represented by Prepetition Compensation, and Prepetition Benefits are needed to enable
13 the Debtor's employees to meet their own personal obligations, they would suffer
14 economic hardship and, in many instances, serious financial difficulties if the relief
15 requested herein is not granted.

16 In light of the foregoing, the Debtor respectfully submits that the payment of the
17 employee-related obligations, including the Expenses, as requested herein is (i) in the best
18 interests of the Debtor, its estate and its creditors and (ii) necessary to prevent immediate
19 and irreparable harm to the Debtor, its estate and their employees.

20 Bankruptcy Courts in this district have routinely approved the payment of
21 prepetition claims of employee wages, salaries, expenses and benefits in various chapter
22 11 cases. *See, e.g., In re Prime Time Int'l Co.*, Case No. 14-03518 [DE 56] (MCW); *In re*
23 *PRM Family Holding Co.*, Case No. 13-09026 [DE 31] (SSC); *In re Basha's Inc.*, Case
24 No. 09-16050 [DE 52] (JMM); *In re Apache Junction Hosp., LLC d/b/a Arizona Regional*
25 *Med. Ctr.*, Case No. 13-18188 [DE. 42] (SHG).

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27 ///

1 **D. The Debtor Requests Immediate Relief and Waiver of Stay**

2 Under Bankruptcy Rules 6003(b) and 6004(h), the Debtor seeks (i) immediate
3 entry of an order granting the relief sought herein and (ii) a waiver of any stay of the
4 effectiveness of such an order. Bankruptcy Rule 6003(b) provides, in pertinent part, that
5 “[e]xcept to the extent that relief is necessary to avoid immediate and irreparable harm,
6 the court shall not, within 21 days after the filing of the petition, grant relief regarding . . .
7 a motion to pay all or part of a claim that arose before the filing of the petition.” FED. R.
8 BANKR. P. 6003(b). Consequently, where the failure to grant any such requested relief
9 would result in immediate and irreparable harm to the Debtor’s estate, the Court may
10 allow the Debtor to pay all or part of a claim that arose before the Petition Date prior to
11 the twenty-first day following the Petition Date. Bankruptcy Rule 6004(h) provides that
12 “[a]n order authorizing the use, sale, or lease of property other than cash collateral is
13 stayed until the expiration of 14 days after entry of the order, unless the court orders
14 otherwise.” FED. R. BANKR. P. 6004(h).

15 As set forth above and in the Gonzales Declaration, the payment of the Prepetition
16 Compensation and Prepetition Benefits is necessary to prevent the immediate and
17 irreparable damage to the Debtor’s (i) operations and (ii) going-concern value that would
18 result from a collapse of Employee morale. The Debtor therefore submits that ample
19 cause exists to justify (i) the immediate entry of an order granting the relief sought herein
20 and (ii) a waiver of the fourteen-day stay imposed by Bankruptcy Rule 6004(h), to the
21 extent that it applies.

22 **IV. CONCLUSION**

23 WHEREFORE, the Debtor respectfully requests that the Court enter an order
24 granting the relief sought herein; and granting the Debtor such other and further relief as
25 the Court may deem proper.

26 ///

27 ///

1 RESPECTFULLY SUBMITTED this 26th day of October, 2018.

2 **MAY, POTENZA, BARAN & GILLESPIE,**
3 **P,C.**

4 By s/ Grant L. Cartwright

5 Grant L. Cartwright

6 Andrew A. Harnisch

7 *Proposed Counsel for Debtor*

8
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